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IN THE

Supreme Court of the United States

OCTOBER TERM, 1937

No. 38

FIDELITY & DEPOSIT COMPANY OF MARYLAND,
Petitioner,

vs.

LOUIS H. PINK, Superintendent of Insurance of the State of New York, as Liquidator of the Southern Surety Company of New York,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENT

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INDEX.

PAGE

STATEMENT OF CASE 1

SUMMARY OF RESPONDENT'S ARGUMENT 4

POINT I—The petitioner is liable upon the reinsurance agreement to the extent of one-half of the liability of the insolvent company in liquidation. Proof of payment is no prerequisite to a recovery by the reinsured's Liquidator 4

CONCLUSION—The judgment below should be affirmed with costs 33

TABLE OF CASES

Aetna Casualty & Surety Co. et al. v. International Reinsurance Co., 117 N. J. Eq. 190 29

Allemannia Fire Ins. Co. v. Firemen's Ins. Co., 209 U. S. 326 ..... 3, 4, 6, 8, 12, 15, 16, 18, 20, 21, 22, 33

Barney v. Preferred Auto, Inc., 240 Mich. 199, 208 24

Blackstone v. Allemannia Fire Ins. Co., 56 N. Y. 104 8

Capelle v. U. S. Fidelity & Guaranty Co., 80 N. H. 481 24

Castellain v. Preston, 11 Q. B. D. 380 29

Cunningham et al. v. Republic Ins. Co. et al., 127 Texas 499 29

Globe Nat. Fire Ins. Co. v. American Bonding & Casualty Co., 198 Iowa 1092 ..... 20, 21, 22, 31

Herckenrath v. American Mutual Ins. Co., 3 Barb. Ch. (N. Y.) 63 9

Hicks v. Poe, 269 U. S. 118 ..... 7, 31

Hone v. Mutual Safety Ins. Co., 3 N. Y. Super. Ct. (1 Sanf.) 137 (affd. 2 N. Y. 235) 8

PAGE

Jackson v. St. Paul Fire & Marine Ins. Co., 99 N. Y. 124, 129-130 31

Morris & Co. et al. v. Skandinavia Ins. Co., 279 U. S. 405 7

Poe v. Munich Reinsurance Co., 276 Fed. 949, 953 (D. C. Md.) 24

Royal Ins. Co. v. Vanderbilt Ins. Co., 102 Tenn. 264 ..... 20, 31

U. S. in Use, etc. v. Federal Surety Co., 72 F. (2d) 964, 967 (C. C. A. 4th Cir.) 31

Yonkers & New York Fire Ins. Co. v. Hoffman Fire Ins. Co., 29 N. Y. Super. Ct. (N. Y.) 316 16

STATUTES AND AUTHORITIES, ETC.

14 R. C. L. 1452 7

8 L. R. A. (N. S.) 862 7

33 C. P., p. 54, Sec. 734 9

Vance on Insurance, 2d Ed. 1930, pp. 942, 946 10

Couch's Cyc. of Insurance Law, Sec. 2277, Vol. 8 10

Cooley's Briefs on Insurance (2d Ed.), p. 6750, Vol. 7 11

50 Harvard Law Review, pp. 95-96 11

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BRIEF FOR RESPONDENT.

Statement of Case.

The facts which gave rise to this action are not in dispute, and were stipulated in writing in the District Court (R. [illegible] They were made the Court's special findings of fa[illegible]. 16).

In the statement set forth at the beginning of petitioner's brief, there appear to be omissions of certain facts which the respondent deems material and pertinent to the points which he makes in this brief, and he therefore sets them forth below in somewhat greater detail.

The respondent is the Superintendent of Insurance of the State of New York and is the Liquidator of the Southern Surety Company of New York, which up to March 22, 1932, was authorized, as a corporation organized in the State of New York, to do a surety and insurance business. On the last mentioned date, by an order of the Supreme Court of the State of New York, made, entered and filed in the office of the County Clerk of New York, the company was declared insolvent, its charter annulled and title to its assets vested in the Superintendent of Insurance of the State of New York, as liquidator thereof, with instructions to liquidate the company (R. 25).

The Southern Surety Company of New York, in the regular course of business and before the entry of the order of liquidation, had issued its fidelity bond to one John DeMartini Co., Inc., wherein it bound itself to indemnify the said John DeMartini Co., Inc., for any pecuniary loss which the latter might sustain through the fraudulent or dishonest acts of its employees during the terms of said bond. While such bond was in effect, an employee, one Marvin Goldblatt, committed fraudulent and dishonest acts within the meaning of the bond, whereby the assured sustained a loss amounting to $7,045.41, for which it filed a proof of loss with the Southern Surety Company of New York. At the time of the entry of the order of liquidation, the claim of John DeMartini Co., Inc., was in the process of examination and investigation by the company, and after the entry of the order of liquidation, the claim was allowed in the liquidation proceeding (R. 18).

On the day Southern Surety Company of New York issued its fidelity bond to John DeMartini Co., Inc., the petitioner reinsured the Southern to the extent of one-half of its liability on said bond not to exceed the sum of $5,000 subject to the terms of a general reinsurance agreement entered into between the petitioner and the Southern on or about the 1st day of April, 1930 (R. 48 and R. 41).

The suit to recover the petitioner's share of the risk was resolved in favor of the respondent by the District Court who brushed aside the contention of the petitioner that, under the terms of the reinsurance agreement, actual payment of the loss to the DeMartini Company was a prerequisite to a recovery and that the reinsurer's liability was limited to the extent of one-half of the amount actually paid. The learned District Judge observed, citing cases, that the question presented had "been determined adversely to the contention of the defendant (petitioner) in a long line of decisions, which have consistently held that under an ordinary agreement of reinsurance, the obligation of a reinsurer is to indemnify the assured not against payment actually made but against liability actually incurred"; and that the attempts of the petitioner to distinguish the cases cited from the instant case on the ground the agreements are dissimilar, were abortive, and said that "a careful comparison of the present agreement with the agreement in *Allemannia* v. *Firemen's* (*supra*) discloses no essential difference insofar as the question under consideration is concerned", and after referring to the similar clauses, concluded that "no departure from the settled law of the *Allemannia* case was intended" (R. 57).

The Circuit Court of Appeals for the Second Circuit unanimously affirmed the judgment on the authority of the *Allemannia* case, among others, and in answer to one of petitioner's contentions said that petitioner, in entering into the reinsurance agreement, undertook "to accept the hazard of the loss, and why it should be able to interpose as a condition the continued ability of the reinsured to meet its part of the obligations is not clear. Of course if it so stipulated, it may insist; but it must stand upon its contract, no general considerations of equity make in its favor" (R. 81).

Summary of Respondent's Argument.

Reinsurance is and always has been held to be an agreement by the reinsurer to indemnify the reinsured against the whole or a proportionate share of the latter's liability to its primary assured. The payment of the reinsurer's obligation to the reinsured is not dependent upon the ability of the latter to pay its assured. The reinsurer having entered into an agreement for which it received a consideration should not be permitted to avail itself of the misfortune of the reinsured as a shield with which to avoid payment of its obligation. The ill fortune of the reinsured in no way diminished or affected the consideration received by the reinsurer.

The reinsurance agreement involved herein shows no intention on the part of the parties to subvert the well settled and universally understood obligations of a reinsurer. Moreover, the circumstances surrounding the drawing of such agreement and its similarity to the reinsurance agreement in the case of *Allemannia Fire Ins. Co.* v. *Firemen's Ins. Co.*, 209 U. S. 326, and other reinsurance pacts, conclusively manifest an intention to abide by and be bound by the rule of law therein enunciated and reiterated.

POINT I

The petitioner is liable upon the reinsurance agreement to the extent of one-half of the liability of the insolvent company in liquidation. Proof of payment is no prerequisite to a recovery by the reinsured's Liquidator.

The petitioner's argument, summarized, is that the reinsurance agreement sued upon is one of indemnity against loss, and, since the respondent has made no *actual* payment to the primary assured on his loss under the bond issued by the now insolvent reinsured, the respond-

ent cannot recover from the reinsurer the latter's proportionate share of its liability therefor. It contends that the language of the agreement sued upon makes payment by the reinsured a condition precedent to recovery by the Liquidator. No case cited by petitioner in its brief sustains this contention.

The respondent submits that the agreement is one of insurance against liability and that the petitioner became liable for its proportionate share of the risk as soon as the insolvent reinsured's liability to its assured became fixed; that neither actual payment of the loss nor notice of intention to pay is a condition precedent to recovery from the petitioner.

In approaching the primary question, i.e., the nature of reinsurance (the subject and object of the agreement), the inquirer is confronted with a line of cases and authorities holding squarely that reinsurance imposes a liability upon the reinsurer whether or not the direct writer pays the loss to its assured.

The words "reinsurance" and "reinsure" have well recognized meanings. They relate to the cession by one insurance company to, and the assumption by another of, all or part of a risk undertaken by the former. The words are instinct with a promise by the reinsurer to indemnify the ceding or reinsured company against liability on its original risk as to the whole or a *pro rata* portion thereof. If the meaning of these terms is to be changed from their universal interpretation of insurance against liability, to indemnity against loss, the intention of the parties to do so should be demonstrated clearly and unequivocally.

No intention to make such a change in the case at bar is patent. Furthermore, the agreement and the circumstances surrounding and preceding its nascency, together with the countless authorities bearing on the question, establish conclusively that the parties intended to follow the construction which had been placed on reinsurance contracts from time immemorial, and that, in letter, as

well as in spirit, the agreement in question is one to insure against liability and not to indemnify against loss.

Allemannia Fire Ins. Co. v. *Firemen's Ins. Co.*, 209 U. S. 326, is directly in point. The plaintiff had issued its policy of fire insurance and had reinsured a portion of its risk with the defendant company. The plaintiff's assured suffered a loss, and before such loss or any part thereof was paid, the plaintiff was rendered insolvent by reason of heavy losses sustained in a great fire in the City of Baltimore in February, 1904. A receiver was appointed for the plaintiff by reason of such insolvency, and he instituted an action against the defendant to recover the proportionate share of plaintiff's liability. Defendant contended that the receiver had paid a dividend of but 55 percent of its liability and maintained that it was liable only for the proportionate share of the loss *actually paid* and not that for which the plaintiff became liable to its assured. Mr. Justice PECKHAM, who wrote the unanimous opinion for the Court, said (p. 332):

> "The term 'reinsurance' has a well-known meaning. That kind of a contract has been in force in the commercial world for a long number of years, and it is entirely different from what is termed 'double insurance', i.e., an insurance of the same interest. The contract is one of indemnity to the person or corporation reinsured, and it binds the reinsurer to pay to the reinsured the whole loss sustained in respect to the subject of the insurance to the extent to which he is reinsured. It is not necessary that the reinsured should first pay the loss to the party first insured before proceeding against the reinsurer upon his contract. The liability of the latter is not affected by the insolvency of the insured * * *. *The claim of the reinsured rests upon its liability to pay its loss to the original insured, and is not based upon * * * ability to pay* * * *." (Italics ours.)

This Court reaffirmed that rule later and held further that *the amount that the reinsured will eventually pay is*

neither a complete nor partial defense to an action brought against the reinsurer upon its contract.

> "There is a further contention that, because the United has not paid to its creditors any part of the amounts due on its contracts, and is likely to pay only twenty-five cents on the dollar, the Munich is under no liability to pay to it anything on account of the losses incurred thereunder or, in any event, more than a *pro rata* share of the payments actually made by the United. The Munich became a reinsurer. *The liability of a reinsurer is not affected by the insolvency of the reinsured company or the inability of the latter to fulfil its own contracts with the original insured.*" (Citing cases.) (Italics ours.)
>
> *Hicks* v. *Poe*, 269 U. S. 118, 120-121.

The theory of the petitioner, if adopted, would change in its entirety the well settled law of reinsurance and leave in its wake the utmost confusion. It would, for example, result in an effect entirely unprecedented with regard to a company which had reinsured all of its outstanding business, transferring the whole of its assets to the reinsuring company as a consideration for such reinsurance. If the argument of the petitioner were advanced to a logical conclusion, the reinsurer would have received all of the assets of the direct writer as consideration for a promise which it could never be called upon to fulfill because the reinsured would have no assets with which to satisfy the loss of an assured. Its inability to satisfy such a loss and produce proof of payment thereof, would relieve the reinsurer from its obligation to the reinsured, to the detriment and prejudice of policyholders of the reinsured, who could in no event recover against the reinsured.

> *Morris & Co. et al.* v. *Skandinavia Insurance Co.*, 279 U. S. 405.
> 14 *R. C. L.* 1452.
> 8 *L. R. A.* (N. S.) 862.

One of the earliest cases on the subject of reinsurance in this country is *Hone* v. *Mutual Safety Ins. Co.*, 3 N. Y. Super. Ct. (1 Sanf.) 137, (affd. 2 N. Y. 235), cited with approval by this Court in the *Allemannia* case, *supra*. Judge SANFORD delineates therein the history of the subject and says (p. 145):

> "For more than two centuries, the conduct of reinsurance has been well known, and its principles firmly established; and we have not met with a single treatise or decision which deviates from the uniform doctrine maintained on the point in question."

The opinion points out that reinsurance contracts were for a long time illegal in England because they were thought to encourage speculation in the rise and fall of premiums and that all of the ancient treatises were by French jurists. He cites Emerigon as the highest authority, and the subject "of the eloquent eulogy of Chancellor Kent", and continues (p. 145):

> "That in case of loss, he (the reinsurer) is held to pay the whole amount for which he is reinsurer without any regard to the circumstances that the reassured may have procured an abatement from the first assured, or may be unable because of bankruptcy to pay the latter in full."

And later (p. 146) states:

> "the same principle is maintained in this country".

In *Blackstone* v. *Allemannia Fire Ins. Co.*, 56 N. Y. 104, the Court of Appeals of the State of New York commended Judge SANFORD'S opinion in the *Hone* case, *supra*, and said (p. 107):

> "In regard to the latter branch of the clause in question, which says that the loss is payable 'at the same time with the reinsured', it is not possible to conclude from it that actual payment by the reinsured is, in fact, to precede or to accompany pay-

ment by the reinsurer. It looks to the time of payability and not to the fact of payment * * *. *To give to it the construction contended for by the defendant would, in substance, subvert the whole contract of reinsurance as hitherto understood in this State.*" (Italics ours.)

In *Herckenrath* v. *American Mutual Insurance Co.*, 3 Barb. Ch. (N. Y.) 63, the reinsurer was held (reporter's headnote) "bound to pay the amount which the original insurer becomes legally liable to pay to the assured in consequence of the risk assumed and not merely the amount which the original insurer actually pays in consequence of the risk assumed by him".

Corpus Juris, in discussing the right of an insolvent reinsured to recover the proportionate share of its liability from a solvent reinsurer, sets forth the rule:

> "The liability of the reinsurer is not affected by the fact that reinsured is insolvent and unable to fulfil his own contract with the person originally insured, the reason being that the *claim of reinsured on the reinsurer rests on the former's liability to pay the loss to the person originally insured, and not on the quantum of his ability to pay it. This is true, notwithstanding a condition in the policy of reinsurance that, in case of loss, the reinsurer shall pay pro rata at the same time, and in the same manner, as reinsured.* And, even though the original insured has received but a small dividend from the estate of the insolvent insurer, the reinsurer is nevertheless liable to pay reinsured's trustee or receiver the whole amount of the reinsurance, and this without deducting the dividend. This also is true even where the reinsurance policy contains the reinsurance clause, for this clause does not prevent reinsured from recovering from the reinsurer as soon as the loss happens and before the former has paid his losses." (Italics ours.)

33 *C. J.*, p. 57, Sec. 734.

A text writer defines the reinsurer's obligation as follows:

> "The reinsurer agrees to indemnify the assured not against payment actually made, but against liability actually incurred; therefore it is by no means that the insurer shall first have paid a loss incurred as a condition precedent to his demanding payment of the reinsurer."
>
> *Vance on Insurance*, 2d Ed. 1930, pp. 942, 946.

Another text writer, under the heading "Accrual of right to sue reinsurer", states:

> "Although the reinsurer is bound under a valid contract of reinsurance, when the reinsured has been found liable or the loss adjusted, the latter may wait until suit has been brought and judgment obtained by the insured before seeking such indemnity from the reinsurer. Furthermore, before the reinsured can recover, it must show either that it has paid a claim under a risk carried by it upon the subject insured, and which has been destroyed or damaged by a cause insured against, or that it has become liable to pay the same, for *it is not necessary that the insured should have paid the loss before proceeding against the reinsurer, it being permissible to bring suit as soon as the liability occurs*, at least where the contract is one of indemnity against the liability of the insurer for loss, it being sufficient that such liability to pay for the loss exists, since *such a contract does not go to the insurer's payment of, or ability to pay, the loss.* For instance, where a company transfers its stock to a reinsuring company upon a guaranty that its obligations to its policyholders shall be fulfilled, some liability to such policyholders must accrue before any action lies upon such guaranty, but when the reinsurer passes into a receiver's hands, and the claims of the policyholders are presented and established, the guaranty should be turned into assets to meet the claims of creditors." (Italics ours.)
>
> *Couch's Cyc. of Insurance Law*, Sec. 2277, Vol. 8.

Mr. Cooley in his *Briefs on Insurance* says:

> "The liability of the company reinsuring accrues at the same time with the liability of the reinsured (Blackstone v. Alemannia Fire Ins. Co., 4 Daly [N. Y.] 299), and **it is not necessary for the reinsured to pay the loss to the first insured before proceeding against the reinsurer.**" (Emphasis ours.)
>
> *Cooley's Briefs on Insurance* (2d Ed.), p. 6750, Vol. 7.

The subject was discussed in the November, 1936, issue of the *Harvard Law Review*, where it was said:

> "The contract of reinsurance has been universally construed as a contract of indemnity against liability rather than one against loss. Hence the liability of the reinsurer to the reinsured accrues immediately upon the reinsured's becoming liable to the insured. Payment of the insured is, therefore, not a condition precedent to the reinsured's right of recovery, and as a result the insured may avail itself of that asset of the reinsured by garnishment. Ordinarily the question of recovery by the insured against the reinsurer becomes important only in cases where the reinsured is insolvent. Although the insolvency of the reinsured has prevented it from paying the insured more than a fraction of its claim, the courts which have dealt with the problem, partly because of an apprehension of mathematical difficulties giving rise to a multiplicity of suits, but mainly following the logical implications of the rule that payment of the insured is not necessary to recovery by the reinsured, have unanimously held the reinsured's right of recovery unaffected by its insolvency."
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> 50 *Harvard Law Review*, pp. 95-96.[1]

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[1] The "mathematical difficulties giving rise to a multiplicity of suits" referred to, would follow petitioner's revolutionary theory. The Liquidator could only recover from the reinsurer its proportionate share of every dividend *after* payment by him. Each dividend payment would signal the institution of a new suit against the reinsurer.

"If the assignee can only recover from the defendant when and as he pays dividends on the assigned estate, to the original insured, it is plain an

The petitioner brushes aside the *Allemannia* case and other authorities referred to here and in the opinions of the Courts below, respectively, asserts that they do not control and avers that the agreement upon which this action is predicated differs from the reinsurance agreements in the cited cases. The contention is a specious one. Those agreements may differ in appearance or verbiage, but are one in substance, in effect and in intent with the agreement in the instant case.[1]

The contract of reinsurance in the *Allemannia* case, *supra,* does not differ in substance from the contract of reinsurance in the case at bar, and the pertinent clauses are hereinafter set forth in parallel columns to illustrate the similarity between the contracts of reinsurance in the instant case and in the *Allemannia* case, *supra,* as compacts of indemnity against *liability* for loss and not against loss.

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endless number of suits must be the consequence; and if it has so happened that there was no assigned estate, there would be no recovery at all. I would construe the words 'as the latter company may pay' to mean 'as the latter company may be liable to pay'." (*In re Fame Ins. Co., Nisi Prius,* Sharwood, J., affd. *In re Fame Ins. Co. Appeal,* 83 Pa. 396, 398.)

An attempt to overcome the mathematical difficulties was made in an article (15 *Harvard Law Review* 866 [1902]) which was intended to present a solution of the difficulty involved in the multiplicity of transactions by the use of a mathematical formula to determine the amount of reinsurance *collectible.* It was conceded the formula, if workable, was applicable only if the doctrine of reinsurance as universally accepted was interpreted as indemnity against loss rather than indemnity against liability. The impracticability of any such formula is apparent by the wide gap existing between computing the amount "collectible" and amount "collected". If the amount collectible from the "A" company is $10,000 and a computation is based thereon in accordance with the formula, and the "A" company before that amount is collected becomes insolvent so that the $10,000 cannot be collected and only a small uncertain dividend in the far distant future is in view, or becomes recalcitrant and refuses to pay, thereby involving unforeseen legal expenses as well as delays, or interposes various defenses and offsets which will take years to litigate and makes the result of such action uncertain, what would happen to the computation? Multiply this instance a few hundred or thousand times and absolute chaos results. The exact and immediate justice that the formula was intended to work out would be absent.

[1] The very agreement sued upon here (R. 47) was passed upon by the Circuit Court of Appeals, Fourth Circuit, as late as 1934, and was held to be one of insurance against liability and not against loss. *United States in Use, etc.* v. *Federal Surety Co. et al.,* 72 Fed. (2d) 964, 967.

Contract of Reinsurance in the Allemannia Case.

"10. Upon receiving notice of any loss or claim under any contract hereunder reinsured, the said reinsured company shall promptly advise the said Allemannia Fire Insurance Company, at Pittsburg, Pennsylvania, of the same, and of the date and probable amount of loss or damage, and after said reinsured company shall have adjusted, accepted proofs of, or paid such loss or damage, it shall forward to the said Allemannia Fire Insurance Company, at Pittsburg, Pennsylvania, a proof of its loss and claim against this company, upon blanks furnished for that purpose by said Firemen's Insurance Company, together with a copy of the original proofs and claim under its contract reinsured, and a copy of the original receipt taken upon the payment of such loss; and, upon request, shall exhibit and permit copies to be made of all other papers connected therewith, which may be in its possession.

"11. Each entry under this compact, unless otherwise provided in this contract, shall be subject to the same conditions, stipulations, risks and valuation as may be assumed by the said reinsured company under its original contracts hereunder reinsured, and losses, if any, shall be payable *pro rata* with, in the same manner, and upon the same terms and conditions, as paid by

Contract of Reinsurance in the Instant Case.

"4. The Reinsured, upon the receipt at its home office of a notice of any claim or loss under the bond, shall give the Reinsurer prompt written notice thereof at the Reinsurer's home office. The term 'home office', wherever used herein, shall be deemed to mean the home office in the United States. The Reinsured shall take charge of all matters arising under the bond in connection with claims. It shall decide whether or not it is liable thereunder, and shall determine the amount of its liability in case it decides that it is liable. It shall settle or compromise any claims and defend, settle, or compromise any suits, and take such other action, not involving the extension of credit or the advancing of money, in connection with any claim matter arising under the bond as it may deem advisable. Any such decision, determination, settlement, defense, compromise or other action of the Reinsured in connection with any claim matter arising under the bond shall be final and conclusive and unconditionally binding upon the Reinsurer; provided that no payment or other method of settlement by the Reinsured shall preclude the Reinsurer from showing that the alleged liability or any part thereof for loss under the bond exists or existed under some other bond or bonds given at any time by the Reinsured.

the said reinsured company under its contracts hereunder reinsured; and in no event shall this company be liable for an amount in excess of a ratable proportion of the sum actually paid to the assured or reinsured by the said reinsured company under its original contracts hereunder reinsured, after deducting therefrom any and all liability of other reinsurers of said contracts or any part thereof."

"The Reinsured's authority to handle and settle claims in accordance with its own judgment as outlined above shall not be annulled, abridged, or otherwise affected, if the Reinsured consults the Reinsurer, by letter, in conference, or otherwise, with reference to such handling and settling of claims; provided that the reservation of rights on the part of the Reinsured effected by this paragraph shall apply only to matters and questions, the sole determination of which is left by this agreement in the hands of the Reinsured.

"If any loss hereunder shall be settled, wholly or in part, through the issuance by the Reinsured of a surety bond, the Reinsurer shall participate in such bond in the proportion defined in section 2 hereof.

"The Reinsurer's proportionate share of a loss under the bond, of costs and expenses as hereinafter defined, and of interest, shall be paid to the Reinsured upon proof of the payment of such items by the Reinsured, and upon delivery to the Reinsurer of copies of all essential documents concerned with such loss and costs and the payment thereof. The Reinsured may, however, give the Reinsurer written notice of its intention to pay the loss on a certain date, and may require the Reinsurer to have its share of such loss in the hands of the Reinsured by such date; provided, however, that the Reinsurer in any event shall have a period of forty-eight hours,

> after the receipt of such written notice from the Reinsured, to mail or otherwise despatch its payment; and provided further that in any such case the Reinsurer, if it desires to do so, may pay its share of the loss by means of a check drawn in favor of the obligee of the bond."

In the *Allemannia* case, Clause 10 required prompt notification, in the event of a loss by the assured of a reinsured, and the forwarding to the reinsurer of various papers "and a copy of the original receipt taken upon the payment of such loss."[1] Clause 11 provided that the reinsurance agreement was to be subject to the same conditions, stipulations and risks as were assumed by the reinsured under its original policy "and loss if any shall be payable *pro rata* with, in the same manner, and upon the same terms and conditions as paid by the reinsured * * * and in no event shall this company be liable for an amount in excess of a ratable proportion of *the sum actually paid* to the assured * * * by the said reinsured company under its original contract hereunder insured."[2]

In the instant case the analogous clause provides that "the reinsurer's proportionate share of a loss under the bond * * * shall be paid to the reinsured upon proof of payment * * * by the reinsured, and upon delivery to the reinsurer of copies of all essential documents * * *." The

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[1] This provision is obviated in the case at bar by the clause that any settlement or adjustment made by the reinsured shall be binding upon the reinsurer (R. 49, lines 58-65), thereby eliminating the necessity for a proof of loss or the "receipt taken upon the payment of such loss".

[2] In the *Blackstone* case, *supra*, the reinsurance contract provided: "Loss, if any, payable *pro rata* and at the same time with the reinsured." It was there held that the contention that the reinsurer was not compelled to pay its share, except contemporaneously and simultaneously with the reinsured, was not tenable.

A similar clause in another contract of reinsurance was construed the same way, the Court ruling that insolvency is no defense to a suit against the reinsurer, that the "condition means that the defendant shall pay at and in the same time and manner as the reinsured company shall pay or be bound to pay according to its policy." *Cashau* v. *Northwestern Nat. Ins. Co.*, 5 Biss. 476, Fed. Cas. No. 2499 (C. C., E. D. Wisc.).

reinsured is required to give prompt written notice of any claim. The requirement as to the forwarding of papers or documents is omitted and, in place thereof, the reinsured is given *carte blanche* with respect to the settlement of any claim except "that no payment or other method of settlement by the reinsured shall preclude the reinsurer from showing that the *alleged liability or any part thereof for loss* under the bond exists or existed under some other bond or bonds given at any time by a reinsurer" (R. 47, lines 64-65).

As in the *Allemannia* case, where the liability of the reinsurer was limited to a ratable proportion *"of the sum actually paid"*, so in the case at bar the reinsurer's proportionate share of the loss is required to be paid upon "proof of payment". The provision in the *Allemannia* case requiring a receipt for the payment of the loss to be produced when demand was made for the proportionate share by the reinsured evoked this explanation by Mr. Justice PECKHAM (p. 337):

> "that if the loss or claim has been in fact paid, then a copy of the receipt is to be sent; but *it does not mean that there must be payment before any liability on the part of the reinsuring company exists.*" (Italics ours.)

To the same effect:

> *Yonkers & New York Fire Ins. Co.* v. *Hoffman Fire Ins. Co.*, 29 N. Y. Super. Ct. [N. Y.] 316.

The petitioner argues that an exception to the requirement for payment is contained in the agreement in the case at bar by that portion which permits the reinsured to give written notice of intention to pay the loss and requesting payment of the reinsurance by such date; that under the construction of both Courts below this clause is surplusage, because if the reinsured could demand payment of the reinsurer without being required to pay as a condition precedent, such a clause is wholly unnecessary.

The petitioner misconstrues the purpose of that clause. Its aim is not to give a means to the reinsured of requiring payment without first paying the loss itself. Its value lies in the elimination of book entries by reinsureds and being compelled to carry a system of debits and credits with reinsurers. It is not surplusage and is not intended as an alternative method, but rather as a convenience. Clearly, it does not and cannot apply to an insolvent company in liquidation, because no notice of that kind could in good faith be given by a liquidator or receiver, for the carrying out of any such intention would involve an unlawful preference. The giving of notice with no intention of carrying it out would be looked at askance, and if carried out, would be subject to attack for illegality.

To further illustrate the speciousness of petitioner's contention, let us assume that the reinsured as a going company had given notice to the reinsurer of intention to pay, etc., and that the reinsurer had, pursuant thereto, forwarded a check for its share directly to the obligee of the reinsured, or to the reinsured in favor of the obligee of the bond; that upon the receipt thereof the reinsured had sent its draft for the balance of the loss, together with the draft of the reinsurer, to such obligee; that before the check of the reinsured cleared, an insolvency petition was filed against the reinsured, a receiver appointed, and its bank account attached, as a result of which the obligee was able to cash the reinsurer's check alone and to content himself with filing a claim against and receiving not the full amount of the balance of his loss, but dividends thereon from the reinsured. What claim would the reinsurer have had either against the obligee or against the reinsured?

The petitioner as reinsurer is placed in no less advantageous position now than it would have been had it been requested to pay its share of the risk to the reinsured if the latter had continued in business. *It is only being called upon to pay that which it agreed to pay for a premium without regard to the ability of the reinsured to pay its assured.*

The precursor of the "Standard Form of Reinsurance Agreement adopted by the Surety Association of America, 1-15-30" (R. 47), involved in the instant case, was the "Standard Form of Reinsurance Agreement adopted by the Surety Association of America, May 12, 1915" (R. 49), but seven years after the handing down of the *Allemannia* decision by this Court. The language of that agreement with respect to the giving of notice of intention to pay is almost precisely the same as is used in the agreement sued upon. Parallel columns are employed in order to show the similarity:

Language Used in the Standard Form of Reinsurance Involved in the Instant Case.	Language Used in the Standard Form of Reinsurance Agreement Adopted in 1915.
"• • • The Reinsured may, however, give the Reinsurer written notice of its intention to pay the loss on a certain date, and may require the Reinsurer to have its share of such loss in the hands of the Reinsured by such date; provided, however, that the Reinsurer in any event shall have a period of forty-eight hours, after the receipt of such written notice from the Reinsured, to mail or otherwise despatch its payment; and provided further that in any such case the Reinsurer, if it desires to do so, may pay its share of the loss by means of a check drawn in favor of the obligee of the bond" (R. 47, lines 74-79).	"• • • The Reinsured may, however, give the Reinsurer at least ten days' written notice of its intention to pay the loss on a certain date, and may require the Reinsurer to pay its proportionate share of such loss before such date; but in that case the Reinsurer, if it desires to do so, may pay its share of the loss by means of a check drawn in favor of the obligee under the bond" (R. 49, lines 36-39).

And, just as the agreement in the case at bar "does hereby reinsure • • • against loss", so also the Standard Form of Agreement adopted in 1915 "does hereby reinsure • • • against loss". The corresponding provisions of these two agreements are subjoined in parallel columns:

Language Used in the Standard Form of Reinsurance Involved in the Instant Case.

"IN CONSIDERATION of the premium payable under section 1 hereof

hereinafter called the REINSURER, does hereby reinsure FIDELITY AND DEPOSIT COMPANY OF MARYLAND, hereinafter called the REINSURED, under bond numbered , together with all riders attached thereto, hereinafter called the BOND, issued by the Reinsured in the penalty of Dollars, in favor of (obligee), and in behalf of , hereinafter called the Principal, against loss thereunder and against costs and expenses, as hereinafter defined, and interest. A copy of the bond is or may be attached hereto, and is hereby made a part of this agreement" (R. 47).

Language Used in the Standard Form of Reinsurance Agreement Adopted in 1915.

"IN CONSIDERATION of the premium stated in section 1 hereof , hereinafter called the Reinsurer, does hereby reinsure the Fidelity and Deposit Company of Maryland, hereinafter called the Reinsured, under bond numbered hereinafter called the bond, issued by the Reinsured in the penalty of Dollars, in favor of (obligee) and in behalf of (principal), against loss thereunder and against costs and expenses, as hereinafter defined. A copy of the bond is or is to be attached hereto, and is hereby made a part of this agreement" (R. 49).

There are other similarities too numerous to mention, which are apparent from a most cursory examination. The agreement sued upon (R. 47) is merely an amplification of the 1915 Standard Form (R. 49). Fundamentally and basically, they are the same.

The 1915 Standard Form was judicially considered in 1923, seven years before the Standard Form involved in the present case was adopted. *This twin brother of the agreement involved in the case at bar was held to be an agreement to insure against liability and not against loss, the Court holding that recovery could be had by the receiver of an insolvent reinsured without prior payment*

of the loss, under that agreement, and that such recovery from the reinsurer was for the benefit of general creditors:

> "The right of the receiver to recover is challenged upon the ground that the insolvent surety has discharged no part of its liability upon the bond executed for the benefit of appellee, and that, as it has suffered no loss, no recovery can be had in the name of the receiver. The contrary appears to be the well-settled rule. The reinsurance contracts are contracts of indemnity, and the receiver *is entitled to recover under the issues and facts of this case, either, for the benefit of general creditors without the prior payment of the loss insured upon the bond.*" (Italics ours.)
>
> *Globe Nat. Fire Ins. Co.* v. *American Bonding & Casualty Co.*, 198 Iowa 1072.

The case of *Royal Ins. Co.* v. *Vanderbilt Ins. Co.*, 102 Tenn. 264, cited by the petitioner as an authority for *its* interpretation of the word "loss" in reinsurance agreements, is of interest in illustrating the wisdom of the opinions below in the case at bar. The construction of the word "loss" there, revolved about a clause in the reinsurance agreement barring an action by the reinsured for recovery of any claim "* * * unless such action shall be commenced within twelve months next ensuing after the loss shall occur". The petitioner there urged that the loss referred to was the loss of the primary assured, and such loss having occurred more than twelve months prior to the institution of the action by the reinsured against the reinsurer, the reinsured was out of court. The Court said (p. 270):

> "Its contention is that the loss it insured against was a loss by fire. This is a mistake. *It indemnified, to a limited extent, against the liability which the first insurer assumed by his contract,* * * *.*" (Italics ours.)

The similarity of the reinsurance agreement in the *Allemannia* case with the Standard Form of 1930 involved

in the present case (R. 47) and both with the Standard Form adopted May 12, 1915 (R. 49), is most striking and leads to the conclusion that there was no intention on the part of the *Surety Association of America, the sponsors of the Standard Form of Reinsurance Agreement adopted in 1915 as well as that adopted in 1930,* to deviate from or change the rule of law with respect to agreements of reinsurance, which through the centuries had been treated as contracts of indemnity against liability and had been reaffirmed as such by this Court in 1908 in *Allemannia* v. *Firemen's Insurance Co., supra,* and other cases.

The marked resemblance of the 1915 and 1930 Standard Forms of Reinsurance has been commented upon, as has also the fact that the 1915 Standard Form (R. 49) was drawn but seven years after the *Allemannia* decision. Eight years later, in 1923, the Supreme Court of Iowa analyzed the 1915 Standard Form in a controversy wherein the petitioner contended that such agreement was one of indemnity against loss and not against liability. The Court unequivocally held that it was one of insurance against liability, wherein the insolvent reinsured was not required to make payment to the primary assured before seeking recovery from the reinsurer of the latter's proportionate share of the risk.

Globe National Fire Insurance Co. v. *American Bonding and Casualty Co., supra.*

Seven years later, in 1930, the Standard Form of Reinsurance Agreement upon which the instant action is predicated was adopted (R. 47), which, in form as well as in substance, is, with the exception of a few added refinements, precisely the same as was the Standard Form of 1915 (R. 49).

It is submitted that if it had been the intention of the sponsors of the Standard Form of 1915 (R. 49), drawn seven years after the decision of this Court in the *Allemannia* case, or its successor, the Standard Form of

1930 involved herein (R. 47), drawn seven years after the decision of the Iowa Supreme Court in the *Globe* case, *supra,* or if it had been the purpose of the parties to the 1930 Standard Form in the case at bar, to evade or avoid the ruling in the *Allemannia* case, holding that a reinsurance compact was an agreement for indemnity against liability and not against loss, and to evade or avoid the ruling in the *Globe* case that the 1915 Standard Form of Reinsurance Agreement was a contract for indemnity against liability and not against loss, it is reasonable to assume that they would have manifested such intent in unmistakable terms, would not have used the same language as was used in the 1915 Standard Form, *would not even have used the word "reinsure",*[1] and would have squarely said that the parties intended that the reinsurer should not be liable and should not be called upon to pay its *pro rata* share of the loss suffered by the reinsurer, unless and until the reinsured had made payment of the loss to its assured, that the reinsured should only be liable in such an event for its pro rata portion of the amount actually paid; and that *no action could be brought by the reinsurer unless instituted within a certain time after actual payment.*[2]

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[1] This word, so pregnant with the definition of insurance against liability, might have been replaced by the word "indemnify" or other language which had not from the beginning of reinsurance contracts been identified with insurance against liability and *never* with indemnity against loss.

[2] The contention of the petitioner that there was no proof that the Surety Association of America had any knowledge of the *Allemannia* case or the decision of the Supreme Court of Iowa in the *Globe* case, is specious. If an association of surety companies which drew and sponsored an agreement for use by all surety companies in America did not keep itself apprised of such far-reaching decisions which affected so many companies and did not make a search for and consider all adjudications bearing upon such an agreement, what did it do? Who would give any weight to an agreement covering such a widely litigated topic without a study of all the cases theretofore decided and the cases thereafter decided construing the same? The appellate court below commented on this phase of the petitioner's argument and stated that while perhaps such a body did not acquaint itself with the decisions of every state, for which reason the Court forbore relying upon *Globe National Fire Ins. Co.* v. *American Bonding & Casualty Co.,* 198 Iowa 1072, that "it is probable that that decision also was known. * * * But to say that the only decision of the Supreme Court upon the point was not known or was not regarded, seems to us to pass any reasonable possibility" (R. 81).

Clause 9 of the reinsurance agreement sued upon (R. 47) is particularly significant in showing that the parties did not intend actual payment by the reinsured to be a condition precedent to the right of recovery against the reinsurer. It provides that "No action shall be brought against the reinsurer hereunder unless brought within twelve months after the date of the final *settlement* of all obligations under the bond." It does not require final *payment* of all obligations or liquidation of all obligations or discharge of all obligations; *it refers merely to a settlement.* The identical clause is found in the 1915 Standard Form (R. 49, lines 75-76). If "final settlement" in the 1915 Standard Form was not construed to mean payment by the Iowa Court; it is submitted that no basis exists now for changing its meaning or asserting that its transposition, without change of accompanying words, into the 1930 Standard Form has altered its meaning.[1] As used in the earlier Standard Form construed by the Court in other reinsurance agreements and in the reinsurance agreement in the case at bar, the implication carried by the word "settlement" is not that of payment, but of adjustment or fixing of the amount of liability.

The term "final settlement" has been judicially defined as meaning not payment, but a determination of the amount due:

> "It argues that final 'settlement' here means payment. So to hold would run counter to the whole scheme of the agreement between the companies. What the Munich assumed was one-third of the liability * * *. The words 'final settlement', as used in this contract, must be held to mean the fixing by agreement or judicial determination of the amount

[1] Webster's New International Dictionary defines the word "settlement" as the "Act of process of adjustment or determining, composure of doubts or differences. Arrangement, adjustment * * *." The verb "settle" is defined as "To adjust differences or accounts; to come to an agreement * * *." In Bouvier's Law Dictionary, the word "settlement" is defined in contracts as "An agreement by which two or more persons who have dealings together so far arrange their accounts as to ascertain the balance due from one to the other * * *." The verb "settle" is there defined as "To adjust or ascertain."

due by the United on the bonds or policies for which the Munich assumed a one-third liability."

Poe v. *Munich Reinsurance Co.*, 276 Fed. 949, 953 (D. C. Md.).

In an action involving a liability policy where the question arose as to whether the policy was one of indemnity against liability or loss, the policy was construed as a policy of insurance against liability, in the absence of a clause prohibiting the assured from bringing action thereon unless he had made actual payment of judgment against him thereunder. The Court said:

"If it was appellant's purpose to insure against loss actually sustained and not against liability, it could have made it plain by a 'no action' clause in unquestionable language familiar to insurance companies and to courts."

Barney v. *Preferred Auto, Inc.*, 240 Mich. 199, 208.

Similarly, where a clause limiting the right of action did not refer to *payment*, but provided that "No action by the assured shall be taken against the company until the amount of damages * * * is determined by final judgment", it was held that such a policy was one of insurance against liability and not against loss.

Capelle v. *U. S. Fidelity & Guaranty Co.*, 80 N. H. 481.

The Courts have uniformly held, as above illustrated, that unless the "no action" clause requires *payment* before action may be instituted, in clear and unmistakable language, the policy will be construed as one of insurance against liability and not loss.

The District Court so held in the case at bar when, in discussing the use of this word, it indicated that the word "settlement" could be used in other ways, but that as used in the agreement it meant determination and not the pay-

ment of a liability, and remarked that *"if it had been intended to make actual payment of the claim a prerequisite to recovery where the reinsured was in liquidation, it is reasonable to assume that unequivocal language to that effect would have been used"* (R. 58).

There was nothing particularly novel about reinsured companies becoming insolvent and going into liquidation at the time of the adoption of the 1930 Standard Form involved here. The majority of cases hereinbefore cited and all of the texts which had been written were concerned with the claims of insolvent reinsureds or their receivers against solvent reinsurers and the right of the former to recover the *pro rata* share of risks from the reinsurers *without first making actual payment* to the primary assureds. It is not reasonable to assume that a subject which had been so widely discussed by Courts and text writers did not leave its impress upon the parties and the sponsors of the Standard Forms of Reinsurance Agreement drafted in 1915 and 1930, and cause them, if indeed they wished to evade such a uniform and time-old construction, to manifest their desire in plain language whereby their intent would be the object of no doubt.

The words "final settlement", even divorced from all judicial determinations and definitions, must be construed in the 1930 Standard Form sued upon as a determination of the amount due, or fixation of liability of the reinsured, and not payment.

Clause 4 of such agreement (R. 47, lines 56-84) provides for the giving of notice by the reinsured to the reinsurer of any claim under the bond, taking charge of matters in connection therewith, and contains the language which the petitioner relies upon to sustain its position that the agreement, notwithstanding all other factors and decisions, is one of indemnity against loss rather than liability.

This clause, in referring to the obligation of the reinsured to "take charge of all matters arising under the bond in connection with claims" and to decide its liability, determine the amount thereof, "settle or compromise any

claims and defend, settle or compromise any suits", further provides that "Any such decision, determination, settlement, defense, compromise, or other action of the reinsured * * * shall be final and conclusive and unconditionally binding upon the reinsurer provided that no payment or other method of settlement by the reinsurer shall preclude the reinsurer from showing *that the alleged liability * * * for loss * * * exists* or existed under some other bond * * *" (R. 47, lines 62-65). (Italics ours.)

Can there be anything more conclusive than the clause so quoted in demonstrating that the agreement is one to insure against liability and not against loss? If no right against the reinsurer were to accrue unless and until the reinsurer made payment to its primary assured or suffered an actual loss, this provision would be utterly inane, because the reinsurer would never be called upon to show that the *"alleged liability * * * for loss* under the bond *exists * * * under some other bond * * * given at any time by the Reinsured"*; the reinsured, having made no payment, could not press its claim against the reinsurer and create the necessity for the interposing of such a defense. The clause refers to the reinsured's "alleged liability or any part thereof for loss under the bond" and unequivocally shows that the parties and the draftsmen of the agreement contemplated a claim or suit by the reinsured against the reinsurer, *not after payment* by the reinsured of a loss under its bond, *but while an alleged liability for loss "exists"*.

It will be further noted that the words "settlement" and "payment" are treated as separate and distinct nouns in the agreement and convey two separate and distinct methods of fixing the amount of the reinsured's liability which in turn fixes the reinsured's liability (R. 47, lines 62-65).

Further evidence of what the parties and the draftsmen of the agreement intended may be found in Section 12 of the agreement sued upon, where reference is made to the reinsurer's liability "on account of any losses", the losses contemplated being those of the *assured* of the re-

insured for which the reinsured might become liable (R. 47, lines 136-138). Provision is further made for liability "for losses which occurred before the effective date of the cancellation of such superseded reinsurance, notification of which was not received by the reinsured" (lines 148-151). The satisfaction of that liability to the reinsured is deferred only to the time when the amount of the liability of the reinsured becomes fixed and determined. Nothing therein requires payment as a prerequisite.

Under Clause 14 every premium payable by the reinsured to the reinsurer is an absolute obligation whether or not the reinsured shall collect from its own debtor the premium on the bond (R. 47, lines 170-171), and "The validity of this agreement shall be in nowise impaired or affected by the failure of the Reinsured, for any cause to pay the Reinsurer either the initial premium or any subsequent premium due from the Reinsurer to the Reinsured" (R. 47, lines 183-184).

Still further evidence of the intent of the parties and the draftsmen is found in the clauses wherein the parties agree to divide salvage which the reinsurer may recover in the proportion that each bears to the risk (R. 47, lines 124-125, 16-21).

The petitioner has misconstrued these provisions and contends that because they fix the division of salvage in the proportion of their respective risks, it follows that the reinsurer's obligation is limited to payment of its proportionate share of the amount paid by the reinsured, because the purpose is to give them "proportionate reimbursement for their respective contributions".

In its deduction, petitioner clearly errs. Indemnity agreements commonly exacted by surety companies as collateral security are agreements to indemnify against liability and not against loss; and in the liquidation of insurance companies, thousands of such indemnity agreements have been sued upon where the liability became fixed, long before the payment of any dividend was ever made or contemplated.

The provisions with respect to salvage not only do not indicate that the reinsurer's liability to the reinsured is dependent upon actual payment by the latter, but are convincing proof to the contrary.

The agreement provides that "The Reinsurer shall be entitled to share with the Reinsured in the proportion defined in section 2 hereof any collateral security or indemnity held by the Reinsured, or any right of action possessed by the Reinsured, in connection with the bond. The Reinsurer and the Reinsured shall share any salvage or recovery * * * in the proportion defined in section 2 hereof" (R. 47, lines 124-127). Section 2 provides that "The Reinsurer's total liability hereunder is limited to * * *; but the Reinsurer shall in no event be liable for a greater proportion * * * than the proportion that the amount of reinsurance bears to the amount of the bond" (R. 47, lines 16-20). (The bond referred to is the bond issued by the reinsurer to its primary assured [R. 47, lines 4-10].)

It is significant that the salvage to which the reinsurer is entitled *is not limited in amount* and it is given the right to share therein in *"the proportion* that the amount of reinsurance bears to the amount of the bond".

If the position of the petitioner were sustained, it might lead to such reinsurer being compensated and enriched far beyond any loss which it might sustain, for its liability would be measured by the amount of dividends paid by the liquidator of the reinsured, whereas it would have the right to salvage for a proportionate share of its *liability* under the bond regardless of the amount which it paid.

Translated into concrete terms, if the liquidator was to recover salvage of $7,000 under an indemnity agreement wherein the indemnitor agreed to indemnify the direct writer (reinsured) against liability, the reinsurer would be entitled to receive the sum of $3,500, which would be its proportion of the salvage recovered, based upon its 50 percent liability under the agreement. If

the liquidator only paid a first and final dividend of 20 percent to general creditors, assuming that the loss of the primary assured was $7,000, and the payment of the liquidator to the primary assured was but $1,400, the reinsurer's share of the loss would be but $700. It would, therefore, make a profit of $2,800 on the transaction in addition to having received and retained a premium from the reinsured in consideration of its reinsuring the risk. Such a situation would hardly be consonant with the theory of reinsurance, the profit in which is presumed to lie in the premium, and salvage in which is intended to minimize loss and not enrich the reinsurer.

This brings the writer to another phase of petitioner's argument. It urges that an affirmance of the judgment of the Court below will permit the Southern to realize a profit out of the reinsurance which would be inconsistent with the fundamental principles thereof and, in support of such contention, it cites the case of *Castellain* v. *Preston*, 11 Q. B. D. 380, which is not applicable to the case at bar, involved no reinsurance and stands for the proposition that a marine or fire insurance policy is a contract of indemnity only, under which a loss shall be fully indemnified and never more than fully indemnified. Of course, no quarrel can be had with the rule of law so enunciated. The case at bar is not concerned with a marine or fire policy or any other kind of a policy such as there described. It revolves about a reinsurance agreement which is *not* a policy of insurance.

Cunningham et al. v. *Republic Insurance Co. et al.*, 127 Texas 499.

Aetna Casualty & Surety Co. et al. v. *International Reinsurance Co.*, 117 N. J. Eq. 190.

Nor does the question of profit at all enter. The *Southern* cannot make a profit. It is dissolved and out of business and its affairs and estate are being administered by the Superintendent of Insurance of the

State of New York, as liquidator thereof, for the benefit of creditors (R. 25).

In the case of an insolvent reinsured, the recovery of the full share from the reinsurer is not barred by the fact that the reinsured has not paid or will not pay its creditors or its primary assured mentioned in the reinsurance agreement in full (see citations and authorities, *supra*).

Certainly, there is no reason, let alone a good reason, why the petitioner should be permitted to take advantage of the misfortune of the reinsured. The latter in no way failed to perform any of the terms, covenants and conditions of the contract between the insolvent company and the reinsurer on the part of the insolvent company to be performed (R. 23).

Precisely why the petitioner, with respect to whom all the terms and conditions of the contract have been performed, should be privileged to take advantage of the misfortune of the reinsured, *which has in no way affected it, is difficult to comprehend.*

The petitioner entered into a reinsurance agreement under which it received a premium from the reinsured as a consideration for assuming the proportionate share of a risk up to and not exceeding a certain amount. A loss under the bond issued by the reinsured having occurred, the reinsurer is only being called upon to do that which it agreed to do for a consideration, viz: pay its proportionate share of the risk.

Why should the reinsured's misfortune, which has in no way injured the reinsurer and has not tended to diminish or wipe out the consideration which the latter received, excuse such reinsurer from the performance of the agreement?

> "• • • The original contract of insurance remained as at first, and the reinsurer came under no contract obligation to the owner of the property described in it. The subsequent act of the insurer did not create any. *Its own risk was the sole object of*

reinsurance and formed the consideration of a new and independent contract, distinct from and unconnected with the original insurance. This is so stated in the policy of reinsurance. It covers in terms the plaintiff's 'interest as insurers' under their policy; *and that alone is made the subject-matter of insurance.*

When, therefore, the Paterson Company was found to be legally liable upon its contract and the amount was ascertained, *it was not open to the reinsurer to inquire into the merits of those questions. They were at once bound to pay the reinsured such a proportion of the loss as their reinsurance bore to the sum originally insured.*" (Italics ours.)

Jackson v. *St. Paul Fire and Marine Ins. Co.*, 99 N. Y. 124, 129-130.

The reinsurer is liable in such a case, even though it received no consideration and might receive nothing therefor, because the reinsurance was linked with a participation contract under which the reinsurer received no premium, but participated in the profits and shared the losses.

Hicks v. *Poe*, 269 U. S. 118.

The money recovered is not for the benefit of the reinsured, but for the benefit of the general creditors.

Royal Ins. Co. v. *Vanderbilt*, 102 Tenn. 264.
Globe Nat. Fire Ins. Co. v. *American Bonding & Casualty Co.*, 198 Iowa 1072.
U. S. in Use, etc. v. *Federal Surety Co.*, 72 F. (2d) 964, 967 (C. C. A. 4th Cir.).

The petitioner advances the further contention that the construction placed upon the reinsurance agreement would permit and induce the liquidator of an insolvent company to concede liability for unfounded claims so as to make a profit by collecting the full *pro rata* share from the reinsurer and thus deprive the reinsurer of protection;

that it will remove any necessity on the part of the liquidator to resist unfounded claims and enable him to make a profit for the defunct company; that the motive underlying the requirement to exercise diligence in protecting the reinsurer would thus be swept away.

The propriety and validity of the allowance by the Liquidator to the assured of the direct writer has been conceded (R. 24) and the *bona fides* of his act is not in issue.

The language of the reinsurance agreement (R. 47) which makes the "decision, determination, settlement, defense, compromise, or other action of the Reinsured in connection with any claim matter arising under the bond * * * final and conclusive and unconditionally binding upon the reinsurer" (R. 47, lines 62-63), does not and cannot by the widest stretch of the imagination be interpreted so as to preclude the reinsurer from resisting payment to the reinsured (or, in the case of insolvency, to the receiver) on the ground of fraud or negligence.

Assuming, *arguendo,* that the purpose of the agreement is to give the reinsured a motive to exercise diligence in protecting the reinsurer from unfounded claims, as is contended by the petitioner, this motive is not nullified by insolvency, but is merged in the higher and broader motive *and duty* of a receiver or liquidator to resist all unfounded claims, not merely for the benefit of the reinsurer or the reinsured, but for the benefit of all creditors of the reinsured and others interested in the estate thereof. If he does not perform his duties in the manner expected of him, and is guilty of fraud or negligence as a result of which the reinsurer is called upon to pay, as its proportionate share of the risk, an amount which might have been considerably less had the receiver or liquidator performed his duty and not been guilty of negligence or fraud, is it not obvious that payment could be resisted and the receiver or liquidator called to account by the reinsurer and the creditors of the insolvent company? The insolvent company in such an event is no more. Any

motive which it might have had in allowing unfounded claims no longer exists. The receiver or liquidator would not benefit by any such negligence or fraud, and would leave himself open to personal liability for any such acts; any moneys recovered by him would inure not to his benefit, but to the benefit of the general creditors of the defunct company.

An express prohibition against fraud may be found in the provision that "This agreement shall be regarded by the parties hereto as an honorable engagement rather than a mere legal obligation * * * " (R. 47, line 185). The District Court referred to this clause as one of the *indicia* of the parties' intent "that no departure from the settled law of the *Allemannia* case was intended" (R. 57).

A reinsurance contract, under all the authorities and texts hereinbefore cited, has been universally accepted and construed as an agreement on the part of a reinsuring company to indemnify a reinsured company against liability on a risk assumed by the latter to its primary assured. The language of the reinsurance pact in the case at bar, and the intention of the draftsmen thereof and the parties thereto, conclusively demonstrate that it was never intended that any fanciful theory or strained construction or interpretation should change or cause any deviation from the well recognized rules and principles of reinsurance as agreements to indemnify against liability and not loss in this and other cases where the 1930 Standard Form is employed.

CONCLUSION

The judgment below should be affirmed with costs.

October, 1937.

Respectfully submitted,

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